

The following table is an analysis of the four largest rebate accruals, which comprise approximately 70 percent of the consolidated rebate provisions charged against revenues in 2008. Remaining rebate provisions charged against gross sales are not significant in the determination of operating earnings. (*dollars in millions*)

	Domestic Pharmaceutical Products			
	Domestic Nutritionals WIC Rebates	Medicaid and Medicare Rebates	Pharmacy Benefit Manager Rebates	Wholesaler Chargebacks
Balance at January 1, 2006	\$ 95	\$ 455	\$ 134	\$ 48
Provisions	637	528	281	533
Payments	(596)	(534)	(246)	(514)
Business combination	—	36	51	20
Balance at December 31, 2006	136	485	220	87
Provisions	754	438	412	786
Payments	(691)	(503)	(395)	(781)
Balance at December 31, 2007	199	420	237	92
Provisions	808	556	397	1,034
Payments	(845)	(681)	(406)	(980)
Balance at December 31, 2008	\$ 162	\$ 295	\$ 228	\$ 146

---

Historically, adjustments to prior years' rebate accruals have not been material to net income. In 2007, adjustments were made to prior years' rebate accruals. The Medicaid and Medicare rebate accrual was reduced by approximately \$69 million and the WIC rebate accrual was increased by approximately \$19 million. Abbott employs various techniques to verify the accuracy of claims submitted to it, and where possible, works with the organizations submitting claims to gain insight into changes that might affect the rebate amounts. For Medicaid, Medicare and other government agency programs, the calculation of a rebate involves interpretations of relevant regulations, which are subject to challenge or change in interpretation.

*Income Taxes* — Abbott operates in numerous countries where its income tax returns are subject to audits and adjustments. Because Abbott operates globally, the nature of the audit items are often very complex, and the objectives of the government auditors can result in a tax on the same income in more than one country. Abbott employs internal and external tax professionals to minimize audit adjustment amounts where possible. On January 1, 2007, Abbott adopted the provisions of FASB Interpretation No. 48 "Accounting for Uncertainty in Income Taxes," which changed the measurement of tax contingencies. Under this Interpretation, in order to recognize an uncertain tax benefit, the taxpayer must be more likely than not of sustaining the position, and the measurement of the benefit is calculated as the largest amount that is more than 50 percent likely to be realized upon resolution of the benefit. Application of this Interpretation requires a significant amount of judgment. In the U.S., Abbott's federal income tax returns through 2005 are settled, and the income tax returns for years after 2005 are open. Abbott does not record deferred income taxes on earnings reinvested indefinitely in foreign subsidiaries.

*Pension and Post-Employment Benefits* — Abbott offers pension benefits and post-employment health care to many of its employees. Abbott engages outside actuaries to assist in the determination of the obligations and costs under these programs. Abbott must develop long-term assumptions, the most

significant of which are the health care cost trend rates, discount rates and the expected return on plan assets. The discount rates used to measure liabilities were determined based on high-quality fixed income securities that match the duration of the expected retiree benefits. The health care cost trend rates represent Abbott's expected annual rates of change in the cost of health care benefits and is a forward projection of health care costs as of the measurement date. A difference between the assumed rates and the actual rates, which will not be known for decades, can be significant in relation to the obligations and the annual cost recorded for these programs. Negative asset returns due to recent poor market conditions and low interest rates have significantly increased actuarial losses for these plans. At December 31, 2008, pretax net actuarial losses and prior service costs and (credits) recognized in Accumulated other comprehensive income (loss) for Abbott's defined benefit plans and medical and dental plans were losses of \$2.6 billion and \$381 million, respectively. Actuarial losses and gains are amortized over the remaining service attribution periods of the employees under the corridor method, in accordance with the rules for accounting for post-employment benefits. Differences between the expected long-term return on plan assets and the actual annual return are amortized over a five-year period. Footnote 5 to the consolidated financial statements describes the impact of a one-percentage point change in the health care cost trend rate; however, there can be no certainty that a change would be limited to only one percentage point. On December 31, 2006, Abbott adopted the provisions of SFAS No. 158 "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans." The provisions of this statement require the recognition of the deferrals on the balance sheet with a corresponding charge to Accumulated other comprehensive income (loss). Adoption of this statement on December 31, 2006 resulted in a decrease in Abbott's shareholders' equity of approximately \$1.3 billion.

*Valuation of Intangible Assets* — Abbott has acquired and continues to acquire significant intangible assets that Abbott records at fair value. Those assets which do not yet have regulatory approval and for which there are no alternative uses are expensed as acquired in-process research and development, and those that have regulatory approval are capitalized. Adoption of SFAS No. 141(R) "Business Combinations" on January 1, 2009 will result in acquired in-process research and development assets

---

acquired in a business combination to be initially recorded as indefinite lived intangible assets. Transactions involving the purchase or sale of intangible assets occur with some frequency between companies in the health care field and valuations are usually based on a discounted cash flow analysis. The discounted cash flow model requires assumptions about the timing and amount of future net cash flows, risk, the cost of capital, terminal values and market participants. Each of these factors can significantly affect the value of the intangible asset. Abbott engages independent valuation experts who review Abbott's critical assumptions and calculations for acquisitions of significant intangibles. Abbott reviews intangible assets for impairment each quarter using an undiscounted net cash flows approach. If the undiscounted cash flows of an intangible asset are less than the carrying value of an intangible asset, the intangible asset is written down to its fair value, which is usually the discounted cash flow amount. Where cash flows cannot be identified for an individual asset, the review is applied at the lowest group level for which cash flows are identifiable. Goodwill is reviewed for impairment annually or when an event that could result in an impairment of goodwill occurs. At December 31, 2008, goodwill and intangibles amounted to \$10.0 billion and \$5.2 billion, respectively, and amortization expense for intangible assets amounted to \$787 million in 2008. There were no impairments of goodwill in 2008, 2007 or 2006.

*Litigation* — Abbott accounts for litigation losses in accordance with SFAS No. 5 "Accounting for Contingencies." Under SFAS No. 5, loss contingency provisions are recorded for probable losses at management's best estimate of a loss, or when a best estimate cannot be made, a minimum loss contingency amount is recorded. These estimates are often initially developed substantially earlier than the ultimate loss is known, and the estimates are refined each accounting period as additional information becomes known.

Accordingly, Abbott is often initially unable to develop a best estimate of loss, and therefore the minimum amount, which could be zero, is recorded. As information becomes known, either the minimum loss amount is increased, resulting in additional loss provisions, or a best estimate can be made, also resulting in additional loss provisions. Occasionally, a best estimate amount is changed to a lower amount when events result in an expectation of a more favorable outcome than previously expected. Except for the cases discussed in footnote 8 for which Abbott is unable to estimate a loss, if any, Abbott estimates the range of possible loss to be from approximately \$255 million to \$495 million for its legal proceedings and environmental exposures. Reserves of approximately \$325 million have been recorded at December 31, 2008 for these proceedings and exposures. These reserves represent management's best estimate of probable loss, as defined by SFAS No. 5.

*Stock Compensation* — Abbott records the fair value of stock options in its results of operations. Since there is no market for trading employee stock options, management must use a fair value method. There is no certainty that the results of a fair value method would be the value at which employee stock options would be traded for cash. Fair value methods require management to make several assumptions, the most significant of which are the selection of a fair value model, stock price volatility and the average life of an option. Abbott has readily available grant-by-grant historical activity for several years in its option administration system that it uses in developing some of its assumptions. Abbott uses the Black-Scholes method to value stock options. Abbott uses both historical volatility of its stock price and the implied volatility of traded options to develop the volatility assumptions. Abbott uses the historical grant activity, combined with expectations about future exercise activity, to develop the average life assumptions. Abbott has also used the historical grant data to evaluate whether certain holders of stock options exercised their options differently than other holders and has not found any differentiating pattern among holders.

## Results of Operations

### Sales

The following table details the components of sales growth by reportable segment for the last three years:

	Total % Change	Components of Change %		
		Price	Volume	Exchange
<b>Total Net Sales</b>				
2008 vs. 2007	13.9	1.4	9.3	3.2
2007 vs. 2006	15.3	1.2	10.9	3.2
2006 vs. 2005	0.6	0.6	0.2	(0.2)
<b>Total U.S.</b>				
2008 vs. 2007	10.1	3.4	6.7	—
2007 vs. 2006	12.0	4.0	8.0	—
2006 vs. 2005	(7.5)	2.4	(9.9)	—
<b>Total International</b>				
2008 vs. 2007	17.8	(0.5)	12.0	6.3

2007 vs. 2006	18.8	(1.7)	14.0	6.5
2006 vs. 2005	10.9	(1.3)	12.7	(0.5)
<b>Pharmaceutical Products Segment</b>				
2008 vs. 2007	14.2	1.9	9.1	3.2
2007 vs. 2006	18.0	2.4	12.3	3.3
2006 vs. 2005	(9.5)	1.8	(11.0)	(0.3)
<b>Nutritional Products Segment</b>				
2008 vs. 2007	12.2	3.4	6.9	1.9
2007 vs. 2006	1.7	1.4	(1.4)	1.7
2006 vs. 2005	9.6	(0.4)	9.7	0.3
<b>Diagnostic Products Segment</b>				
2008 vs. 2007	13.2	1.3	6.8	5.1
2007 vs. 2006	11.1	(0.6)	7.0	4.7
2006 vs. 2005	5.7	(1.1)	7.4	(0.6)
<b>Vascular Products Segment</b>				
2008 vs. 2007	34.7	(4.6)	35.8	3.5
2007 vs. 2006	53.8	(4.7)	55.4	3.1
2006 vs. 2005	327.7	(4.6)	333.2	(0.9)

Worldwide 2008 sales growth compared to 2007 reflects unit growth and the positive effect of the relatively weaker U.S. dollar. Worldwide 2007 sales compared to 2006 reflect the acquisitions of Guidant's vascular intervention and endovascular solutions businesses on April 21, 2006 and Kos Pharmaceuticals Inc. in the fourth quarter of 2006. In addition, the Pharmaceutical Products segment had an agreement with Boehringer Ingelheim (BI) to co-promote and distribute three of its products in the U.S. In 2005, Abbott and BI amended the agreement and effective January 1, 2006, Abbott no longer distributed or recorded sales for distribution activities for the BI products although Abbott recorded a small amount of co-promotion revenue in 2006. The increases in sales for 2006 excluding BI products were

---

11.6 percent for total net sales, 12.3 percent for total U.S. sales and 7.8 percent for Pharmaceutical Products segment sales. Sales growth in 2007 for the Nutritional Products segment reflects the completion of the U.S. co-promotion of *Synagis* in 2006. Excluding sales of *Synagis* in 2006, Nutritional Products segment sales increased 11.3 percent.

A comparison of significant product group sales is as follows. Percent changes are versus the prior year and are based on unrounded numbers.

	2008	Percent Change	2007	Percent Change	2006	Percent Change
<b>Pharmaceuticals</b>						

U.S. Specialty	\$5,211	20	\$4,349	24	\$3,505	25
U.S. Primary Care	3,102	(1)	3,139	23	2,561	4
International Pharmaceuticals	7,399	23	6,002	16	5,157	8
<b>Nutritionals —</b>						
U.S. Pediatric Nutritionals	1,268	3	1,233	9	1,128	3
International Pediatric Nutritionals	1,374	26	1,093	22	899	29
U.S. Adult Nutritionals	1,162	8	1,077	2	1,057	1
International Adult Nutritionals	1,070	13	947	15	824	11
<b>Diagnostics —</b>						
Immunochemistry	2,843	13	2,517	11	2,272	4

Increased sales of *HUMIRA* and the addition of *Lupron* sales in 2008 accounted for the majority of the sales increase for U.S. Specialty products in 2008. Increased sales of *HUMIRA* and *Depakote* accounted for the majority of the sales increases for U.S. Specialty products in 2007 and 2006. U.S. sales of *HUMIRA* were \$2.2 billion, \$1.6 billion and \$1.2 billion in 2008, 2007 and 2006, respectively. U.S. Primary Care sales in 2008 were impacted by a significant decrease in sales of *Omnicef* due to generic competition, partially offset by increased sales of *Niaspan* and the *TriCor/Trilipix* franchise. U.S. Primary Care sales in 2007 were favorably impacted by sales of *Niaspan*, a new product from the acquisition of Kos Pharmaceuticals Inc. in the fourth quarter of 2006. In addition, increased sales of *TriCor* in 2007 and 2006 favorably impacted U.S. Primary Care sales. These increases were partially offset by lower sales of *Omnicef* in 2008 and 2007 and lower U.S. sales of *Biaxin* in all three years due primarily to the introduction of generic competition. U.S. sales of *Omnicef* were \$25 million, \$235 million and \$637 million in 2008, 2007 and 2006, respectively, and U.S. sales of *Biaxin* were \$14 million, \$36 million and \$151 million in 2008, 2007 and 2006, respectively. Increased sales volume of *HUMIRA* in all three years favorably impacted International Pharmaceuticals sales, partially offset by decreased sales volume in 2008 and 2006 due to generic competition for clarithromycin. International sales of *HUMIRA* were \$2.3 billion, \$1.4 billion and \$868 million in 2008, 2007 and 2006, respectively. International Pediatric Nutritionals sales increases were due primarily to volume growth in developing countries. International sales in 2008 and 2007 were also favorably impacted by the effect of the relatively weaker U.S. dollar. Abbott has periodically sold product rights to non-strategic products and has recorded the related gains in net sales in accordance with Abbott's revenue recognition policies as discussed in footnote 1 to the consolidated financial statements. Related net sales were \$111 million, \$184 million and \$199 million in 2008, 2007 and 2006, respectively.

The expiration of licenses, patent protection and generic competition can affect the future revenues and operating income of Abbott. Significant ongoing generic activities and significant patent and license expirations in the next three years are as follows. The U.S. composition of matter patent for *Depakote* expired in 2008. Abbott has seen generic competition begin in the second half of 2008 for *Depakote*, which had U.S. sales of \$1.3 billion in 2008.

---

### Operating Earnings

Gross profit margins were 57.3 percent of net sales in 2008, 55.9 percent in 2007 and 56.3 percent in 2006. The increase in the gross profit margin in 2008 was due, in part, to favorable product mix and the favorable impact of foreign exchange. The decrease in the gross profit margin in 2007 was due, in part, to

the unfavorable impact in 2007 of the completion of the U.S. co-promotion of *Synagis* in 2006 as well as generic competition for *Omnicef* and *Biaxin* sales in 2007. The increase in the gross profit margin in 2006 was due to favorable product mix, primarily as a result of decreased sales of Boehringer Ingelheim products that had lower margins than other products in the Pharmaceutical Products segment. Restructuring charges, discussed below, reduced the gross profit margins in 2008, 2007 and 2006 by 0.4 percentage points, 0.7 percentage points and 1.1 percentage points, respectively. Gross profit margins in all years were also affected by productivity improvements, higher commodity costs, higher project expenses for new products, higher manufacturing capacity costs for anticipated unit growth and the effects of inflation.

In the U.S., states receive price rebates from manufacturers of infant formula under the federally subsidized Special Supplemental Nutrition Program for Women, Infants, and Children. There are also rebate programs for pharmaceutical products. These rebate programs continue to have a negative effect on the gross profit margins of the Nutritional and Pharmaceutical Products segments. Higher commodity costs unfavorably impacted the gross profit margins for the Nutritional Products segment in 2008 and 2007 and pricing pressures unfavorably impacted the gross profit margin in 2006.

Research and development expense, excluding acquired in-process and collaborations research and development, was \$2.7 billion in 2008, \$2.5 billion in 2007 and \$2.3 billion in 2006 and represented increases of 7.3 percent in 2008, 11.1 percent in 2007 and 23.8 percent in 2006. The effect of recording compensation expense relating to share-based awards in 2006 and additional costs associated with Abbott's decision to discontinue the commercial development of the *ZoMaxx* drug-eluting stent increased research and development expenses by 6.3 percentage points over 2005. The increases in 2007 and 2006 were also affected by the acquisitions of Guidant's vascular intervention and endovascular solutions businesses in April 2006 and Kos Pharmaceuticals Inc. in the fourth quarter of 2006. These increases also reflect increased spending to support pipeline programs, including new indications for *HUMIRA*, and *Trilipix*, *Trilipix/Crestor* fixed-dose combination, ABT-874 (a biologic for psoriasis and Crohn's disease), pain relief medication and *Xience V*, as well as several Phase I and Phase II clinical programs in neuroscience, oncology and Hepatitis C. The majority of research and development expenditures are concentrated on pharmaceutical products.

Selling, general and administrative expenses increased 13.9 percent in 2008 compared to increases of 16.7 percent in 2007 and 15.5 percent in 2006. The 2008 increase reflects the settlement of litigation relating to *TriCor*, which increased selling, general and administration expenses by 3.1 percentage points. The 2007 increase reflects the acquisitions of Guidant's vascular intervention and endovascular solutions businesses and Kos Pharmaceuticals Inc. The 2006 increase reflects recording compensation expense relating to share-based awards, a philanthropic contribution to the Abbott Fund and the acquisition of Guidant's vascular intervention and endovascular solutions businesses. These items increased selling, general and administrative expenses by 8.6 percentage points over 2005. The remaining increases in selling, general and administrative expenses were due primarily to increased selling and marketing support for new and existing products, including continued spending for *HUMIRA* and the continuing launch of *Xience V*, as well as spending on other marketed pharmaceutical products. Increases in all three years also reflect inflation and additional selling and marketing support primarily in the Pharmaceutical Products segment.

#### **Conclusion of TAP Pharmaceutical Products Inc. Joint Venture and Sale of Abbott's Spine Business**

On April 30, 2008, Abbott and Takeda concluded their TAP Pharmaceutical Products Inc. (TAP) joint venture, evenly splitting the value and assets of the joint venture. Abbott exchanged its 50 percent equity

interest in TAP for the assets, liabilities and employees related to TAP's *Lupron* business. Subsequent to the conclusion of the joint venture, TAP was merged into two Takeda entities. The exchange of Abbott's investment in TAP for TAP's *Lupron* business resulted in a gain at closing of approximately \$94 million. The Internal Revenue Service has issued a private letter ruling that the transaction qualifies as tax-free for U.S. income tax purposes.

Beginning on May 1, 2008, Abbott began recording U.S. *Lupron* net sales and costs in its operating results and no longer records income from the TAP joint venture. TAP's sales of *Lupron* were \$182 million for the four months ended April 30, 2008 and \$645 million and \$662 million in 2007 and 2006, respectively. Abbott also receives payments based on specified development, approval and commercial events being achieved with respect to products retained by Takeda and payments from Takeda based on sales of products retained by Takeda, which are recorded by Abbott as Other (income) expense, net as earned. Such payments, which are subject to tax, are expected to approximate \$1.4 billion over the five-year period beginning on May 1, 2008.

The exchange transaction was accounted for as a sale of Abbott's equity interest in TAP and as an acquisition of TAP's *Lupron* business under SFAS No. 141 "Business Combinations." The sale of Abbott's equity interest in TAP resulted in the recording of net assets related to the *Lupron* business, primarily cash, receivables, inventory and other assets, net of accounts payable and other accrued liabilities, offset by a credit to Abbott's investment in TAP in the amount of approximately \$280 million.

For the acquired *Lupron* business, Abbott recorded intangible assets, primarily *Lupron* product rights, of approximately \$700 million, goodwill of approximately \$350 million and deferred tax liabilities related primarily to the intangible assets of approximately \$260 million. The intangible assets are being amortized over 15 years. Abbott has also agreed to remit cash to Takeda if certain research and development events are not achieved on the development assets retained by Takeda. These amounts were recorded as a liability at closing in the amount of approximately \$1.1 billion. Related deferred tax assets of approximately \$410 million were also recorded, resulting in an after-tax liability of approximately \$700 million. Of the \$1.1 billion, Abbott made a tax-deductible payment of \$200 million in 2008 and Abbott will make a tax-deductible payment of approximately \$120 million in 2009. If the remaining payments are not required, the liability would be reduced and a gain would be recorded.

The 50 percent-owned joint venture was accounted for under the equity method of accounting. Summarized financial information for TAP follows below. The results for 2008 include results through April 30. (*dollars in millions*)

	Year Ended December 31		
	2008	2007	2006
Net sales	\$853	\$3,002	\$3,363
Cost of sales	229	720	836
Income before taxes	356	1,564	1,524
Net income	238	996	952

In the fourth quarter of 2008, Abbott sold its spine business for approximately \$360 million in cash, resulting in an after-tax gain of approximately \$147 million which is presented as Gain on sale of discontinued operations, net of taxes, in the accompanying statement of income. The operations and financial position of the spine business are not presented as discontinued operations because the effects would not be significant.

#### Restructurings

In 2008, Abbott management approved a plan to streamline global manufacturing operations, reduce overall costs, and improve efficiencies in Abbott's core diagnostic business. This plan will result in pretax charges of approximately \$370 million over the next several years. These charges include employee-related

costs of approximately \$110 million, accelerated depreciation of approximately \$75 million, and other related exit costs of approximately \$185 million, mainly related to product transfers. In 2008, Abbott recorded a charge to Cost of products sold of approximately \$129 million under the plan. Additional charges of approximately \$16 million were recorded in 2008 relating to this restructuring, primarily for accelerated depreciation. The remainder of the charges will occur through 2011 as a result of product re-registration timelines required under manufacturing regulations in a number of countries and product transition timelines. The following summarizes the activity for this restructuring: (*dollars in millions*)

	<u>2008</u>
2008 restructuring charge	\$129
Payments and other adjustments	(19)
Accrued balance at December 31	<u>\$110</u>

In 2008, 2007 and 2006, Abbott management approved plans to realign its worldwide pharmaceutical and vascular manufacturing operations and selected domestic and international commercial and research and development operations in order to reduce costs. In 2008, 2007 and 2006, Abbott recorded charges of approximately \$36 million, \$107 million and \$210 million, respectively, reflecting the impairment of manufacturing facilities and other assets, employee severance and other related charges. Approximately \$94 million and \$181 million in 2007 and 2006, respectively, is classified as cost of products sold, \$3 million and \$29 million in 2007 and 2006, respectively, as research and development and \$36 million and \$10 million in 2008 and 2007, respectively, as selling, general and administrative. Fair value for the determination of the amount of asset impairments was determined primarily based on a discounted cash flow method. An additional \$81 million, \$90 million and \$70 million were subsequently recorded in 2008, 2007 and 2006, respectively, relating to these restructurings, primarily for accelerated depreciation. In addition, Abbott implemented facilities restructuring plans in 2007 related to the acquired operations of Kos Pharmaceuticals Inc., which resulted in an increase to goodwill of approximately \$52 million. Abbott expects to incur up to an additional \$21 million in future periods for these restructuring plans, primarily for accelerated depreciation. The following summarizes the activity for these restructurings: (*dollars in millions*)

	<u>Employee-Related and Other</u>	<u>Asset Impairments</u>	<u>Total</u>
Accrued balance at January 1, 2006	\$ 155	\$ —	\$ 155
2006 restructuring charges	117	93	210
Payments, impairments and other adjustments	(79)	(93)	(172)
Accrued balance at December 31, 2006	193	—	193
2007 restructuring charges	121	38	159
Payments, impairments and other adjustments	(120)	(38)	(158)
Accrued balance at December 31, 2007	194	—	194
2008 restructuring charges	36	—	36
Payments and other adjustments	(125)	(125)	(125)
Accrued balance at December 31, 2008	\$ 105	\$ —	\$ 105

**Interest expense and Interest (income)**

In 2008, interest expense decreased primarily as a result of lower interest rates and interest income increased primarily as the result of higher investment balances. Interest expense increased in 2007 and 2006 due primarily to higher borrowings as a result of the acquisitions of Guidant's vascular intervention and endovascular solutions businesses and Kos Pharmaceuticals Inc. and Abbott's investment in the Boston Scientific common stock and note receivable.

**Other (income) expense, net**

As described above, Abbott recorded a gain of approximately \$94 million in connection with the dissolution of the TAP Pharmaceutical Products Inc. joint venture in 2008, which is included in Other (income) expense, net. Other (income) expense, net for 2008 also includes a gain of approximately \$52 million on the sale of an equity investment accounted for as an available-for-sale investment. The remainder of Other (income) expense, net for 2008 relates primarily to contractual payments based on specified development, approval and commercial events being achieved with respect to products retained by Takeda and payments from Takeda based on sales of products retained by Takeda. Other (income) expense, net for 2007 includes a \$190 million fair market value loss adjustment to Abbott's investment in Boston Scientific common stock and a realized gain of \$37 million on the sales of Boston Scientific common stock. Other (income) expense, net for 2007 and 2006 includes fair value gain adjustments of \$28 million and \$91 million, respectively, to certain derivative financial instruments included with the investment in Boston Scientific common stock.

**Taxes on Earnings**

The income tax rates on earnings from continuing operations were 19.2 percent in 2008, 19.3 percent in 2007 and 24.6 percent in 2006. Taxes on earnings from continuing operations in 2006 reflect the effect of the tax rates applied to acquired in-process research and development and the resolution of prior years' income tax audits and the effect of other discrete tax items. For 2006, the tax rates applied to acquired in-process and collaborations research and development increased the effective tax rate by 6.6 percentage points and the effect of the income tax audit resolution and other discrete tax items decreased the effective tax rate by 5.5 percentage points. Abbott expects to apply an annual effective rate of between 17.5 percent and 18.0 percent in 2009.

**Business Combinations, Technology Acquisitions and Related Transactions**

In December 2006, Abbott acquired Kos Pharmaceuticals Inc. for cash of approximately \$3.8 billion, net of cash held by Kos Pharmaceuticals Inc., to expand Abbott's presence in the lipid management market and to provide several on-market and late-stage pipeline products. Kos Pharmaceuticals Inc. was a specialty pharmaceutical company that developed and marketed proprietary medications for the treatment of chronic cardiovascular, metabolic and respiratory diseases. This business was acquired on December 13, 2006 and the financial results of the acquired operations are included in these financial statements beginning on that date. The acquisition was financed primarily with short-term debt. The allocation of the purchase price resulted in a charge of \$1.3 billion for acquired in-process research and development, intangible assets of \$821 million, goodwill (primarily non-deductible) of \$1.6 billion and net liabilities, primarily deferred income taxes recorded at acquisition of \$331 million. Acquired intangible assets are being amortized over 4 to 15 years. Non-deductible acquired in-process research and development was charged to income in 2006.

In order to expand Abbott's presence in the growing vascular market, Abbott acquired Guidant's vascular intervention and endovascular solutions businesses on April 21, 2006 for approximately \$4.1 billion, in cash, in connection with Boston Scientific's acquisition of Guidant. In addition, Abbott agreed to pay to Boston Scientific \$250 million each upon government approvals to market the *Xience V*

drug-eluting stent in the U.S. and in Japan. In 2008, the FDA approved the marketing of *Xience V* and Abbott paid Boston Scientific \$250 million, resulting in the recording of additional goodwill. Government approval in Japan is anticipated in late 2009 or early 2010 which will also result in the recording of additional goodwill. The allocation of the purchase price resulted in a charge of \$665 million for acquired in-process research and development, intangible assets of \$1.2 billion, goodwill (primarily deductible) of \$1.7 billion and tangible net assets of \$580 million. Acquired intangible assets are being amortized over 4 to 15 years. Deductible acquired in-process research and development was charged to income in 2006. The net tangible assets acquired consist primarily of property and equipment of approximately \$530 million, trade accounts receivable of approximately \$250 million and inventories of approximately \$120 million, net of assumed liabilities, primarily trade accounts payable, litigation reserves and other liabilities.

Had the above acquisitions taken place on January 1 of the previous year, consolidated net sales and income would not have been significantly different from reported amounts.

In order to facilitate Boston Scientific's acquisition of Guidant, Abbott also acquired 64.6 million shares of Boston Scientific common stock directly from Boston Scientific and loaned \$900 million to a wholly-owned subsidiary of Boston Scientific. The common stock was valued at \$1.3 billion and the note receivable was valued at \$829 million at the acquisition date. In connection with the acquisition of the shares, Boston Scientific was entitled to certain after-tax gains upon Abbott's sale of the shares. In addition, Boston Scientific agreed to reimburse Abbott for certain borrowing costs on debt incurred to acquire the Boston Scientific shares. Abbott recorded a net derivative financial instruments liability of \$59 million for the gain-sharing derivative financial instrument liability and the interest derivative financial instrument asset. The effect of recording the shares, the loan to Boston Scientific and the derivative financial instruments at fair value on the date of acquisition resulted in the recording of additional goodwill of approximately \$204 million. Changes in the fair value of the derivative financial instruments, net were recorded in Other (income) expense, net.

#### **Subsequent Event — Business Combination**

In January 2009, Abbott announced an agreement to acquire Advanced Medical Optics, Inc. (AMO), a marketer of ophthalmic surgical technology and devices, as well as eye care solutions, for approximately \$2.8 billion, in cash and debt, to take advantage of increasing demand for vision care technologies due to population growth and demographic shifts. The transaction is expected to close in the first quarter of 2009. AMO's sales are more than \$1 billion per year.

#### **Financial Condition**

##### **Cash Flow**

Net cash from operating activities of continuing operations amounted to \$7.0 billion, \$5.2 billion and \$5.3 billion in 2008, 2007 and 2006, respectively. Cash from operating activities of continuing operations in 2008 compared to 2007 is higher due to higher operating earnings, decreased prepaid expenses and other assets, and increased trade accounts payable and other liabilities. Cash from operating activities of

continuing operations in 2007 and 2006 compared to 2005 is higher due to higher net earnings adjusted for after-tax non-cash charges for acquired in-process research and development in 2006 and share-based compensation and higher contributions to retirement benefit plans in 2005 compared to 2007 and 2006; partially offset by higher income tax payments in 2006, including tax payments related to the 2005 remittances of foreign earnings under the American Jobs Creation Act. Abbott funds its domestic pension plans according to IRS funding limitations. In 2008, 2007 and 2006, \$200 million was funded to the main domestic pension. Abbott expects pension funding for its main domestic pension plan of \$700 million in 2009 and \$200 million annually, thereafter. Abbott expects annual cash flow from operating activities to continue to exceed Abbott's capital expenditures and cash dividends.

### **Debt and Capital**

At December 31, 2008, Abbott's long-term debt rating was AA by Standard & Poor's Corporation and A1 by Moody's Investors Service. Abbott has readily available financial resources, including unused lines of credit of \$5.3 billion that support commercial paper borrowing arrangements of which a \$2.3 billion facility expires in December 2009 and a \$3.0 billion facility expires in 2012. Abbott's access to short-term financing has not been affected by the recent credit market conditions.

In 2006, the board of directors authorized the purchase of \$2.5 billion of Abbott's common shares from time to time and no shares were purchased under this authorization in 2006. In 2008 and 2007, Abbott purchased approximately 19.0 million of its common shares in each period at a cost of approximately \$1.1 billion and \$1.0 billion, respectively under this authorization. Effective in the fourth quarter of 2008, no more purchases of common shares will be made from the 2006 authorization. In October 2008, the board of directors authorized the purchase of up to \$5 billion of Abbott's common shares from time to time and 146,400 shares were purchased under this authorization in 2008 at a cost of approximately \$8 million.

Under a registration statement filed with the Securities and Exchange Commission in February 2006, Abbott issued \$3.5 billion of long-term debt in 2007 that matures in 2012 through 2037 with interest rates ranging from 5.15 percent to 6.15 percent. Proceeds from this debt were used to pay down short-term borrowings that were incurred to partially fund the acquisition of Kos Pharmaceuticals Inc. Under the same registration statement, Abbott issued \$4.0 billion of long-term debt in 2006 that matures in 2009 through 2016 with interest rates ranging from 5.375 percent to 5.875 percent. Proceeds from this debt were used to pay down domestic commercial paper borrowings that were incurred to partially fund the acquisition of Guidant's vascular intervention and endovascular solutions businesses.

In 2009, the acquisition of Advanced Medical Optics, Inc., the funding of Abbott's main domestic pension plan and the payment of long-term debt will be financed with operating cash flow and debt.

### **Working Capital**

Working capital was \$5.5 billion at December 31, 2008 and \$4.9 billion at December 31, 2007. At December 31, 2006, current liabilities exceeded current assets by approximately \$669 million as a result of increased short-term borrowings used to acquire Kos Pharmaceuticals Inc. in December 2006.

### **Capital Expenditures**

Capital expenditures of \$1.3 billion in 2008, \$1.7 billion in 2007 and \$1.3 billion in 2006 were principally for upgrading and expanding manufacturing, research and development, investments in

information technology and administrative support facilities in all segments, and for laboratory instruments placed with customers.

---

### **Contractual Obligations**

The following table summarizes Abbott's estimated contractual obligations as of December 31, 2008:  
(*dollars in millions*)

	<b>Payment Due By Period</b>				
	<b>Total</b>	<b>2009</b>	<b>2010-2011</b>	<b>2012-2013</b>	<b>2014 and Thereafter</b>
Long-term debt, including current maturities and future interest payments	\$13,512	\$1,467	\$2,989	\$1,896	\$ 7,160
Operating lease obligations	416	74	122	88	132
Capitalized auto lease obligations	93	31	62	—	—
Purchase commitments (a)	4,627	4,328	258	32	9
Other long-term liabilities reflected on the consolidated balance sheet					
Benefit plan obligations	3,048	—	714	777	1,557
Other	1,524	—	1,065	198	261
Total	<u>\$23,220</u>	<u>\$5,900</u>	<u>\$ 5,210</u>	<u>\$ 2,991</u>	<u>\$ 9,119</u>

(a)

Purchase commitments are for purchases made in the normal course of business to meet operational and capital expenditure requirements.

### **Contingent Obligations**

Abbott has periodically entered into agreements in the ordinary course of business, such as assignment of product rights, with other companies which has resulted in Abbott becoming secondarily liable for obligations that Abbott was previously primarily liable. Since Abbott no longer maintains a business relationship with the other parties, Abbott is unable to develop an estimate of the maximum potential amount of future payments, if any, under these obligations. Based upon past experience, the likelihood of payments under these agreements is remote. In addition, Abbott periodically acquires a business or product rights in which Abbott agrees to pay contingent consideration based on attaining certain thresholds or based on the occurrence of certain events. In connection with the acquisition of Guidant's vascular intervention and endovascular solutions businesses, Abbott will pay to Boston Scientific \$250 million upon government approval to market the *Xience V* drug-eluting stent in Japan. Government approval is anticipated in late 2009 or early 2010. In addition, Abbott has retained liabilities for taxes on income prior to the spin-off of Hospira and certain potential liabilities, if any, related to alleged improper pricing practices in connection with federal, state and private reimbursement for certain drugs.

### **Recently Issued Accounting Standards**

In 2007, the FASB issued SFAS No. 141 (revised 2007) "Business Combinations" and SFAS No. 160 "Noncontrolling Interests in Consolidated Financial Statements — an amendment of ARB No. 51." Abbott will adopt these standards on January 1, 2009. Statement No. 141 (revised 2007) will impact Abbott primarily in five areas: acquired in-process research and development will be accounted for as an indefinite lived intangible asset until approval or discontinuation rather than as expense; acquisition costs will be

expensed rather than added to the cost of an acquisition; restructuring costs in connection with an acquisition will be expensed rather than added to the cost of an acquisition; the fair value of contingent consideration at the date of an acquisition will be included in the cost of an acquisition; and the fair value of contingent liabilities that are more likely than not of occurrence will be recorded at the date of an acquisition. The effect of these changes will be applicable to acquisitions on or after January 1, 2009. Adoption of Statement No. 160 will not have a material effect on Abbott.

39

---

### **Legislative Issues**

Abbott's primary markets are highly competitive and subject to substantial government regulation throughout the world. Abbott expects debate to continue over the availability, method of delivery, and payment for health care products and services. Abbott believes that if legislation is enacted, it could change access to health care products and services, or reduce prices or the rate of price increases for health care products and services. It is not possible to predict the extent to which Abbott or the health care industry in general might be adversely affected by these factors in the future. A more complete discussion of these factors is contained in Item 1, Business, and Item 1A, Risk Factors, to the Annual Report on Form 10-K.

### **Private Securities Litigation Reform Act of 1995 — A Caution Concerning Forward-Looking Statements**

Under the safe harbor provisions of the Private Securities Litigation Reform Act of 1995, Abbott cautions investors that any forward-looking statements or projections made by Abbott, including those made in this document, are subject to risks and uncertainties that may cause actual results to differ materially from those projected. Economic, competitive, governmental, technological and other factors that may affect Abbott's operations are discussed in Item 1A, Risk Factors, to the Annual Report on Form 10-K.

40

---

### **ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

#### **Financial Instruments and Risk Management**

##### **Investment in Boston Scientific Common Stock and Note Receivable**

At December 31, 2007, Abbott held 26.4 million shares, or approximately \$300 million of Boston Scientific common stock. In 2008 all of these shares were sold resulting in a small gain. Abbott also has a \$900 million loan, due in April 2011, to a wholly-owned subsidiary of Boston Scientific as of December 31, 2008 and 2007, and, as such, is subject to credit risk.

##### **Other Market Price Sensitive Investments**

Abbott holds available-for-sale equity securities from strategic technology acquisitions, excluding Boston Scientific. The market value of these investments was approximately \$105 million and \$193 million, respectively, as of December 31, 2008 and 2007. Abbott monitors these investments for other than temporary declines in market value, and charges impairment losses to income when an other than temporary decline in value occurs. A hypothetical 20 percent decrease in the share prices of these

investments would decrease their fair value at December 31, 2008 by approximately \$21 million. (A 20 percent decrease is believed to be a reasonably possible near-term change in share prices.)

#### **Non-Publicly Traded Equity Securities**

Abbott holds equity securities from strategic technology acquisitions that are not traded on public stock exchanges. The carrying value of these investments was approximately \$42 million and \$37 million as of December 31, 2008 and 2007, respectively. No individual investment is in excess of \$13 million. Abbott monitors these investments for other than temporary declines in market value, and charges impairment losses to income when an other than temporary decline in estimated value occurs.

#### **Interest Rate Sensitive Financial Instruments**

At December 31, 2008 and 2007, Abbott had interest rate hedge contracts totaling \$2.5 billion and \$1.5 billion, respectively, to manage its exposure to changes in the fair value of debt due in 2009 through 2017. The effect of these hedges is to change the fixed interest rate to a variable rate. Abbott does not use derivative financial instruments, such as interest rate swaps, to manage its exposure to changes in interest rates for its investment securities. At December 31, 2008, Abbott had \$1.0 billion of domestic commercial paper outstanding with an average annual interest rate of 0.2% with an average remaining life of 11 days. The fair value of long-term debt at December 31, 2008 and 2007 amounted to \$10.5 billion and \$10.6 billion, respectively (average interest rates of 5.2% and 5.0%, respectively) with maturities through 2037. At December 31, 2008 and 2007, the fair value of current and long-term investment securities amounted to \$1.8 billion and \$896 million, respectively. A hypothetical 100-basis point change in the interest rates would not have a material effect on cash flows, income or market values. (A 100-basis point change is believed to be a reasonably possible near-term change in rates.)

#### **Foreign Currency Sensitive Financial Instruments**

Abbott enters into foreign currency forward exchange contracts to manage its exposure to foreign currency denominated intercompany loans and trade payables and third-party trade payables and receivables. The contracts are marked-to-market, and resulting gains or losses are reflected in income and are generally offset by losses or gains on the foreign currency exposure being managed. At December 31, 2008 and 2007, Abbott held \$8.3 billion and \$5.5 billion, respectively, of such contracts, which mature in the next twelve months.

In addition, certain Abbott foreign subsidiaries enter into foreign currency forward exchange contracts to manage exposures to changes in foreign exchange rates for anticipated intercompany

purchases by those subsidiaries whose functional currencies are not the U.S. dollar. These contracts are designated as cash flow hedges of the variability of the cash flows due to changes in foreign currency exchange rates and are marked-to-market with the resulting gains or losses reflected in Accumulated other comprehensive income (loss). Gains or losses will be included in Cost of products sold at the time the products are sold, generally within the next twelve months. At December 31, 2008 and 2007, Abbott held \$129 million and \$281 million, respectively, of such contracts, which all mature in the following calendar year.

Abbott has designated approximately \$585 million of foreign denominated short-term debt as a hedge of the net investment in certain foreign subsidiaries. Accordingly, changes in the fair value of this debt due to changes in exchange rates are recorded in Accumulated other comprehensive income (loss).

The following table reflects the total foreign currency forward contracts outstanding at December 31, 2008 and 2007: (*dollars in millions*)

	2008			2007		
	Contract Amount	Average Exchange Rate	Fair and Carrying Value Receivable/(Payable)	Contract Amount	Average Exchange Rate	Fair and Carrying Value Receivable/(Payable)
<b>Receive primarily U.S. Dollars in exchange for the following currencies:</b>						
Euro	\$3,963	1.286	\$ 3	\$2,630	1.464	\$ (11)
British Pound	1,208	1.553	(31)	1,030	2.041	—
Japanese Yen	1,788	99.6	54	939	113.9	(5)
Canadian Dollar	163	1.240	3	426	0.995	(1)
All other currencies	1,254	N/A	19	716	N/A	(4)
<b>Total</b>	<b>\$8,376</b>		<b>\$ 48</b>	<b>\$5,741</b>		<b>\$ (21)</b>

---

#### ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

---

	<u>Page</u>
<b>Abbott Laboratories Financial Statements:</b>	
Consolidated Statement of Earnings	44
Consolidated Statement of Cash Flows	45
Consolidated Balance Sheet	46
Consolidated Statement of Shareholders' Investment	48
Notes to Consolidated Financial Statements	49
Management Report on Internal Control Over Financial Reporting	73
Reports of Independent Registered Public Accounting Firm	74
<b>TAP Pharmaceutical Products Inc. Financial Statements:</b>	
Consolidated Statements of Income and Comprehensive Income	76
Consolidated Statements of Cash Flows	77
Consolidated Balance Sheets	78
Consolidated Statements of Shareholders' Equity	79
Notes to Consolidated Financial Statements	80
Report of Independent Registered Public Accounting Firm	92

---

#### Abbott Laboratories and Subsidiaries

---

**Consolidated Statement of Earnings**

(dollars and shares in thousands except per share data)

	<u>Year Ended December 31</u>		
	<u>2008</u>	<u>2007</u>	<u>2006</u>
<b>Net Sales</b>	<b>\$29,527,552</b>	<b>\$25,914,238</b>	<b>\$22,476,322</b>
Cost of products sold	12,612,022	11,422,046	9,815,147
Research and development	2,688,811	2,505,649	2,255,271
Acquired in-process and collaborations research and development	97,256	—	2,014,000
Selling, general and administrative	8,435,624	7,407,998	6,349,685
Total Operating Cost and Expenses	<u>23,833,713</u>	<u>21,335,693</u>	<u>20,434,103</u>
Operating Earnings	5,693,839	4,578,545	2,042,219
Interest expense	528,474	593,142	416,172
Interest (income)	(201,229)	(136,752)	(123,825)
(Income) from TAP Pharmaceutical Products Inc. joint venture	(118,997)	(498,016)	(475,811)
Net foreign exchange (gain) loss	84,244	14,997	28,441
Other (income) expense, net	(454,939)	135,526	(79,128)
Earnings from Continuing Operations Before Taxes	5,856,286	4,469,648	2,276,370
Taxes on Earnings from Continuing Operations	<u>1,122,070</u>	<u>863,334</u>	<u>559,615</u>
Earnings from Continuing Operations	4,734,216	3,606,314	1,716,755
Gain on Sale of Discontinued Operations, net of taxes	146,503	—	—
<b>Net Earnings</b>	<b><u>\$ 4,880,719</u></b>	<b><u>\$ 3,606,314</u></b>	<b><u>\$ 1,716,755</u></b>
<b>Basic Earnings Per Common Share —</b>			
Continuing Operations	\$ 3.06	\$ 2.34	\$ 1.12
Gain on Sale of Discontinued Operations, net of taxes	0.10	—	—
<b>Net Earnings</b>	<b><u>\$ 3.16</u></b>	<b><u>\$ 2.34</u></b>	<b><u>\$ 1.12</u></b>
<b>Diluted Earnings Per Common Share —</b>			
Continuing Operations	\$ 3.03	\$ 2.31	\$ 1.12
Gain on Sale of Discontinued Operations, net of taxes	0.09	—	—
<b>Net Earnings</b>	<b><u>\$ 3.12</u></b>	<b><u>\$ 2.31</u></b>	<b><u>\$ 1.12</u></b>
<b>Average Number of Common Shares Outstanding Used for Basic Earnings Per Common Share</b>	<b>1,545,355</b>	<b>1,543,082</b>	<b>1,529,848</b>
<b>Dilutive Common Stock Options and Awards</b>	<b>15,398</b>	<b>16,975</b>	<b>6,876</b>
<b>Average Number of Common Shares Outstanding Plus Dilutive Common Stock Options and Awards</b>	<b>1,560,753</b>	<b>1,560,057</b>	<b>1,536,724</b>
<b>Outstanding Common Stock Options Having No Dilutive Effect</b>	<b><u>30,579</u></b>	<b><u>6,406</u></b>	<b><u>23,567</u></b>

The accompanying notes to consolidated financial statements are an integral part of this statement.

**Consolidated Statement of Cash Flows**  
**(dollars in thousands)**

	Year Ended December 31		
	2008	2007	2006
<b>Cash Flow From (Used in) Operating Activities of Continuing Operations:</b>			
Net earnings	\$ 4,880,719	\$ 3,606,314	\$ 1,716,755
Less: Gain on sale of discontinued operations	146,503	—	—
Earnings from continuing operations	<u>4,734,216</u>	<u>3,606,314</u>	<u>1,716,755</u>
Adjustments to reconcile earnings from continuing operations to net cash from operating activities of continuing operations—			
Depreciation	1,051,728	1,072,855	983,485
Amortization of intangible assets	787,101	782,031	575,265
Share-based compensation	347,015	429,677	329,957
Gain on dissolution of TAP Pharmaceutical Products Inc. joint venture	(94,248)	—	—
Acquired in-process research and development	97,256	—	1,927,300
Investing and financing (gains) losses, net	111,238	356,331	277,388
Trade receivables	(948,314)	(431,846)	(101,781)
Inventories	(257,476)	131,324	104,653
Prepaid expenses and other assets	436,218	(418,344)	(283,455)
Trade accounts payable and other liabilities	569,056	(82,960)	(183,203)
Income taxes	160,830	(261,539)	(84,275)
<b>Net Cash From Operating Activities of Continuing Operations</b>	<b><u>6,994,620</u></b>	<b><u>5,183,843</u></b>	<b><u>5,262,089</u></b>
<b>Cash Flow From (Used in) Investing Activities of Continuing Operations:</b>			
Contingent consideration paid relating to a business acquisition	(250,000)	—	—
Acquisitions of businesses and technologies, net of cash acquired	—	—	(7,923,163)
Acquisitions of property and equipment	(1,287,724)	(1,656,207)	(1,337,818)
Sales of (investment in) Boston Scientific common stock; and (investments in) note receivable and derivative financial instruments	318,645	568,437	(2,095,780)
Purchases of investment securities	(923,937)	(32,852)	(33,632)
Proceeds from sales of investment securities	130,586	17,830	18,476
Other	(75,061)	(33,485)	(25,712)
<b>Net Cash (Used in) Investing Activities of Continuing Operations</b>	<b><u>(2,087,491)</u></b>	<b><u>(1,136,277)</u></b>	<b><u>(11,397,629)</u></b>
<b>Cash Flow From (Used in) Financing Activities of Continuing Operations:</b>			
(Repayments of) net proceeds from issuance of short-term debt and other	(324,739)	(3,603,481)	5,183,225
Proceeds from issuance of long-term debt	—	3,500,000	4,000,000
Repayments of long-term debt	(913,948)	(441,012)	(3,532,408)
Purchases of common shares	(1,081,806)	(1,058,793)	(754,502)
Proceeds from stock options exercised, including income tax benefit	1,008,843	1,249,804	502,782
Dividends paid	(2,174,252)	(1,959,150)	(1,777,170)
<b>Net Cash (Used in) From Financing Activities of Continuing Operations</b>	<b><u>(3,485,902)</u></b>	<b><u>(2,312,632)</u></b>	<b><u>3,621,927</u></b>

Effect of exchange rate changes on cash and cash equivalents	(115,160)	200,258	73,966
Net cash provided from the sale of discontinued operations in 2008 and from operating activities of discontinued operations of Hospira, Inc. in 2006	349,571	—	67,152
Net Increase (Decrease) in Cash and Cash Equivalents	1,655,638	1,935,192	(2,372,495)
Cash and Cash Equivalents, Beginning of Year	2,456,384	521,192	2,893,687
<b>Cash and Cash Equivalents, End of Year</b>	<b>\$ 4,112,022</b>	<b>\$ 2,456,384</b>	<b>\$ 521,192</b>

The accompanying notes to consolidated financial statements are an integral part of this statement.

### Abbott Laboratories and Subsidiaries

#### Consolidated Balance Sheet (dollars in thousands)

	<b>December 31</b>		
	<b>2008</b>	<b>2007</b>	<b>2006</b>
<b>Assets</b>			
Current Assets:			
Cash and cash equivalents	\$ 4,112,022	\$ 2,456,384	\$ 521,192
Investments, including \$307,500 of investments measured at fair value at December 31, 2007	967,603	364,443	852,243
Trade receivables, less allowances of — 2008: \$263,632; 2007: \$258,288; 2006: \$215,443	5,465,660	4,946,876	4,231,142
Inventories:			
Finished products	1,545,950	1,677,083	1,338,349
Work in process	698,140	681,634	686,425
Materials	531,759	592,725	781,647
Total inventories	2,775,849	2,951,442	2,806,421
Deferred income taxes	2,462,871	2,109,872	1,716,916
Other prepaid expenses and receivables	1,258,554	1,213,716	1,153,969
Total Current Assets	17,042,559	14,042,733	11,281,883
Investments	1,073,736	1,125,262	1,229,873
<b>Property and Equipment, at Cost:</b>			
Land	509,606	494,021	488,342
Buildings	3,698,861	3,589,050	3,228,485
Equipment	10,366,267	10,393,402	9,947,503
Construction in progress	613,939	1,121,328	737,609
	15,188,673	15,597,801	14,401,939
Less: accumulated depreciation and amortization	7,969,507	8,079,652	7,455,504
Net Property and Equipment	7,219,166	7,518,149	6,946,435
Intangible Assets, net of amortization	5,151,106	5,720,478	6,403,619
Goodwill	9,987,361	10,128,841	9,449,281
Deferred Income Taxes and Other Assets	1,945,276	1,178,461	867,081
	<b>\$42,419,204</b>	<b>\$39,713,924</b>	<b>\$36,178,172</b>

**Abbott Laboratories and Subsidiaries****Consolidated Balance Sheet  
(dollars in thousands)**

	December 31		
	2008	2007	2006
<b>Liabilities and Shareholders' Investment</b>			
Current Liabilities:			
Short-term borrowings	\$ 1,691,069	\$ 1,827,361	\$ 5,305,985
Trade accounts payable	1,351,436	1,219,529	1,175,590
Salaries, wages and commissions	1,011,312	859,784	807,283
Other accrued liabilities	4,216,742	3,713,104	3,850,723
Dividends payable	559,064	504,540	453,994
Income taxes payable	805,397	80,406	262,344
Obligation in connection with conclusion of TAP Pharmaceutical Products Inc. joint venture	915,982	—	—
Current portion of long-term debt	1,040,906	898,554	95,276
Total Current Liabilities	<u>11,591,908</u>	<u>9,103,278</u>	<u>11,951,195</u>
Long-term Debt	8,713,327	9,487,789	7,009,664
Post-employment Obligations and Other Long-term Liabilities	<u>4,634,418</u>	<u>3,344,317</u>	<u>3,163,127</u>
Commitments and Contingencies			
Shareholders' Investment:			
Preferred shares, one dollar par value			
Authorized — 1,000,000 shares, none issued	—	—	—
Common shares, without par value			
Authorized — 2,400,000,000 shares	—	—	—
Issued at stated capital amount —			
Shares: 2008: 1,601,580,899; 2007: 1,580,854,677;	—	—	—
2006: 1,550,590,438	7,444,411	6,104,102	4,290,929
Common shares held in treasury, at cost —			
Shares: 2008: 49,147,968; 2007: 30,944,537;	(2,626,404)	(1,213,134)	(195,237)
2006: 13,347,272	—	—	—
Earnings employed in the business	13,825,383	10,805,809	9,568,728
Accumulated other comprehensive income (loss)	(1,163,839)	2,081,763	389,766
Total Shareholders' Investment	<u>17,479,551</u>	<u>17,778,540</u>	<u>14,054,186</u>
	<u>\$42,419,204</u>	<u>\$39,713,924</u>	<u>\$36,178,172</u>

The accompanying notes to consolidated financial statements are an integral part of this statement.

**Consolidated Statement of Shareholders' Investment**  
 (dollars in thousands except per share data)

	Year Ended December 31		
	2008	2007	2006
<b>Common Shares</b>			
Beginning of Year			
Shares: 2008: 1,580,854,677; 2007: 1,550,590,438; 2006: 1,553,769,958	\$ 6,104,102	\$ 4,290,929	\$ 3,477,460
Issued under incentive stock programs			
Shares: 2008: 20,726,222; 2007: 30,264,239; 2006: 14,456,341	1,001,507	1,316,294	526,435
Tax benefit from option shares and vesting of restricted stock awards (no share effect)	64,714	163,808	42,062
Share-based compensation	342,315	433,319	337,428
Issuance of restricted stock awards	(68,227)	(100,248)	(52,392)
Retired — Shares: 2006: 17,635,861	—	—	(40,064)
End of Year			
Shares: 2008: 1,601,580,899; 2007: 1,580,854,677; 2006: 1,550,590,438	<u>\$ 7,444,411</u>	<u>\$ 6,104,102</u>	<u>\$ 4,290,929</u>
<b>Common Shares Held in Treasury</b>			
Beginning of Year			
Shares: 2008: 30,944,537; 2007: 13,347,272; 2006: 14,534,979	\$(1,213,134)	\$(195,237)	\$(212,255)
Private transaction in 2008			
Shares purchased: 15,176,500	—	—	—
Shares issued: 14,870,195	(378,931)	—	—
Issued under incentive stock programs			
Shares: 2008: 1,607,326; 2007: 2,063,123; 2006: 1,197,838	40,946	37,080	17,492
Purchased			
Shares: 2008: 19,504,452; 2007: 19,660,388; 2006: 10,131	<u>(1,075,285)</u>	<u>(1,054,977)</u>	<u>(474)</u>
End of Year			
Shares: 2008: 49,147,968; 2007: 30,944,537; 2006: 13,347,272	<u>\$(2,626,404)</u>	<u>\$(1,213,134)</u>	<u>\$(195,237)</u>
<b>Earnings Employed in the Business</b>			
Beginning of Year			
Net earnings	\$10,805,809	\$ 9,568,728	\$10,404,568
Cash dividends declared on common shares (per share — 2008: \$1.44; 2007: \$1.30; 2006: \$1.18)	4,880,719	3,606,314	1,716,755
Reclassification resulting from the application of the fair value option to Boston Scientific common stock, net of tax	—	(188,534)	—
Cost of common shares retired in excess of stated capital amount	(2,228,776)	(2,009,696)	(1,807,829)
Cost of treasury shares issued below market value	438,221	66,955	35,386
End of Year	<u>\$13,825,383</u>	<u>\$10,805,809</u>	<u>\$ 9,568,728</u>
<b>Accumulated Other Comprehensive Income (Loss):</b>			
Beginning of Year	\$ 2,081,763	\$ 389,766	\$ 745,498
Reclassification resulting from the application of the fair value option to Boston Scientific common stock, net of tax	—	181,834	—
Beginning of Year, as adjusted	2,081,763	571,600	745,498
Other comprehensive (loss) income	(3,245,602)	1,510,163	898,266
Adjustment to recognize net actuarial gain (loss) and prior	—	—	(1,253,998)

service cost as a component of accumulated other comprehensive income (loss), net of tax			
End of Year	\$ (1,163,839)	\$ 2,081,763	\$ 389,766
Comprehensive Income	<u>\$ 1,635,117</u>	<u>\$ 5,116,477</u>	<u>\$ 2,615,021</u>

The accompanying notes to consolidated financial statements are an integral part of this statement.

---

### Abbott Laboratories and Subsidiaries

#### Notes to Consolidated Financial Statements

##### **Note 1 — Summary of Significant Accounting Policies**

**NATURE OF BUSINESS** — Abbott's principal business is the discovery, development, manufacture and sale of a broad line of health care products.

**CONCENTRATION OF RISK AND GUARANTEES** — Due to the nature of its operations, Abbott is not subject to significant concentration risks relating to customers, products or geographic locations, except that three U.S. wholesalers accounted for 27 percent, 25 percent and 23 percent of trade receivables as of December 31, 2008, 2007 and 2006, respectively. Product warranties are not significant.

Abbott has no material exposures to off-balance sheet arrangements; no special purpose entities; nor activities that include non-exchange-traded contracts accounted for at fair value. Abbott has periodically entered into agreements in the ordinary course of business, such as assignment of product rights, with other companies which has resulted in Abbott becoming secondarily liable for obligations that Abbott was previously primarily liable. Since Abbott no longer maintains a business relationship with the other parties, Abbott is unable to develop an estimate of the maximum potential amount of future payments, if any, under these obligations. Based upon past experience, the likelihood of payments under these agreements is remote. Abbott periodically acquires a business or product rights in which Abbott agrees to pay contingent consideration based on attaining certain thresholds or based on the occurrence of certain events. In connection with the spin-off of Hospira, Inc., Abbott has retained liabilities for taxes on income prior to the spin-off and certain potential liabilities, if any, related to alleged improper pricing practices in connection with federal, state and private reimbursement for certain drugs.

**BASIS OF CONSOLIDATION** — The consolidated financial statements include the accounts of the parent company and subsidiaries, after elimination of intercompany transactions. The accounts of foreign subsidiaries are consolidated as of November 30, due to the time needed to consolidate these subsidiaries. No events occurred related to these foreign subsidiaries in December 2008, 2007 and 2006 that materially affected the financial position, results of operations or cash flows.

**USE OF ESTIMATES** — The financial statements have been prepared in accordance with generally accepted accounting principles in the United States and necessarily include amounts based on estimates and assumptions by management. Actual results could differ from those amounts. Significant estimates include amounts for sales rebates, income taxes, pension and other post-employment benefits, valuation of intangible assets, litigation, share-based compensation, derivative financial instruments, and inventory and accounts receivable exposures.

**REVENUE RECOGNITION** — Revenue from product sales is recognized upon passage of title and risk of loss to customers. Provisions for discounts, rebates and sales incentives to customers, and returns and other adjustments are provided for in the period the related sales are recorded. Sales incentives to customers are not material. Historical data is readily available and reliable, and is used for estimating the amount of the reduction in gross sales. Revenue from the launch of a new product, from an improved version of an existing product, or for shipments in excess of a customer's normal requirements are recorded when the conditions noted above are met. In those situations, management records a returns reserve for such revenue, if necessary. Sales of product rights for marketable products are recorded as revenue upon disposition of the rights. Revenue from license of product rights, or for performance of research or selling activities, is recorded over the periods earned.

**INCOME TAXES** — On January 1, 2007, Abbott adopted the provisions of FASB Interpretation No. 48 "Accounting for Uncertainty in Income Taxes." Under this Interpretation, in order to recognize an uncertain tax benefit, the taxpayer must be more likely than not of sustaining the position, and the measurement of the benefit is calculated as the largest amount that is more than 50 percent likely to be

#### **Note 1 — Summary of Significant Accounting Policies (Continued)**

realized upon resolution of the benefit. Deferred income taxes are provided for the tax effect of differences between the tax bases of assets and liabilities and their reported amounts in the financial statements at the enacted statutory rate to be in effect when the taxes are paid. U.S. income taxes are provided on those earnings of foreign subsidiaries which are intended to be remitted to the parent company. Deferred income taxes are not provided on undistributed earnings reinvested indefinitely in foreign subsidiaries as working capital and plant and equipment. Interest and penalties on income tax obligations are included in taxes on income.

**PENSION AND POST-EMPLOYMENT BENEFITS** — Abbott accrues for the actuarially determined cost of pension and post-employment benefits over the service attribution periods of the employees. Abbott must develop long-term assumptions, the most significant of which are the health care cost trend rates, discount rates and the expected return on plan assets. Differences between the expected long-term return on plan assets and the actual return are amortized over a five-year period. Actuarial losses and gains are amortized over the remaining service attribution periods of the employees under the corridor method. On December 31, 2006, Abbott adopted the provisions of SFAS No. 158 "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans." This statement requires recognition of the deferrals on the balance sheet with a corresponding charge to Accumulated other comprehensive income (loss). Adoption of this statement on December 31, 2006 resulted in a decrease in Abbott's shareholders' equity of approximately \$1.3 billion.

**FAIR VALUE MEASUREMENTS** — On January 1, 2007, Abbott adopted SFAS No. 157 "Fair Value Measurements." Adoption of the provisions of this standard did not have a material effect on Abbott's financial position. For assets and liabilities that are measured using quoted prices in active markets, total fair value is the published market price per unit multiplied by the number of units held without consideration of transaction costs. Assets and liabilities that are measured using significant other observable inputs are valued by reference to similar assets or liabilities, adjusted for contract restrictions and other terms specific to that asset or liability. For these items, a significant portion of fair value is derived by reference to quoted prices of similar assets or liabilities in active markets. For all remaining assets and liabilities, fair value is derived using a fair value model, such as a discounted cash flow model or Black-Scholes model. Purchased intangible assets are recorded at fair value. The fair value of significant

purchased intangible assets is based on independent appraisals. Abbott uses a discounted cash flow model to value intangible assets. The discounted cash flow model requires assumptions about the timing and amount of future net cash flows, risk, the cost of capital, terminal values and market participants. Intangible assets and goodwill are reviewed for impairment at least on a quarterly and annual basis, respectively.

**SHARE-BASED COMPENSATION** — The value of stock options and restricted stock awards and units are amortized over their service period, which could be shorter than the vesting period if an employee is retirement eligible, with a charge to compensation expense.

**LITIGATION** — Abbott accounts for litigation losses in accordance with SFAS No. 5. Under SFAS No. 5, loss contingency provisions are recorded for probable losses at management's best estimate of a loss, or when a best estimate cannot be made, a minimum loss contingency amount is recorded.

**CASH, CASH EQUIVALENTS AND INVESTMENTS** — Cash equivalents consist of time deposits and certificates of deposit with original maturities of three months or less. Except for Abbott's investment in the common stock of Boston Scientific, investments in marketable equity securities are classified as available-for-sale and are recorded at fair value with any unrealized holding gains or losses, net of tax, included in Accumulated other comprehensive income (loss). Beginning on January 1, 2007, the investment in the common stock of Boston Scientific was accounted for as a trading security with changes in fair value recorded in income. Investments in equity securities that are not traded on public stock

---

**Note 1 — Summary of Significant Accounting Policies (Continued)**

exchanges are recorded at cost. Investments in debt securities are classified as held-to-maturity, as management has both the intent and ability to hold these securities to maturity, and are reported at cost, net of any unamortized premium or discount. Income relating to these securities is reported as interest income.

Abbott reviews the carrying value of investments each quarter to determine whether an other than temporary decline in market value exists. Abbott considers factors affecting the investee, factors affecting the industry the investee operates in and general equity market trends. Abbott considers the length of time an investment's market value has been below carrying value and the near-term prospects for recovery to carrying value. When Abbott determines that an other than temporary decline has occurred, the investment is written down with a charge to Other (income) expense, net.

**INVENTORIES** — Inventories are stated at the lower of cost (first-in, first-out basis) or market. Cost includes material and conversion costs.

**PROPERTY AND EQUIPMENT** — Depreciation and amortization are provided on a straight-line basis over the estimated useful lives of the assets. The following table shows estimated useful lives of property and equipment:

Classification	Estimated Useful Lives
Buildings	10 to 50 years (average 27 years)
Equipment	3 to 20 years (average 11 years)

**PRODUCT LIABILITY** — Abbott accrues for product liability claims, on an undiscounted basis, when it is probable that a liability has been incurred and the amount of the liability can be reasonably estimated based on existing information. The liabilities are adjusted quarterly as additional information becomes available. Receivables for insurance recoveries for product liability claims are recorded as assets, on an undiscounted basis, when it is probable that a recovery will be realized. Abbott carried third-party insurance coverage in amounts that reflect historical loss experience, which does not include coverage for sizable losses. Subsequent to 2008, product liability losses will be self-insured.

**RESEARCH AND DEVELOPMENT COSTS** — Internal research and development costs are expensed as incurred. Clinical trial costs incurred by third parties are expensed as the contracted work is performed. Where contingent milestone payments are due to third parties under research and development arrangements, the milestone payment obligations are expensed when the milestone results are achieved.

---

**Note 2 — Supplemental Financial Information**

	<u>2008</u>	<u>2007</u>	<u>2006</u>
	(dollars in millions)		
<b>Current Investments</b>			
Time deposits and certificates of deposit	\$ 968	\$ 56	\$ 77
Boston Scientific common stock	—	308	775
<b>Total</b>	<u>\$ 968</u>	<u>\$ 364</u>	<u>\$ 852</u>

	<u>2008</u>	<u>2007</u>	<u>2006</u>
	(dollars in millions)		
<b>Long-term Investments:</b>			
Boston Scientific common stock	\$ —	\$ —	\$ 248
Other equity securities	147	229	130
Note receivable from Boston Scientific, 4% interest, due in 2011	865	851	837
Other	62	45	15
<b>Total</b>	<u>\$1,074</u>	<u>\$1,125</u>	<u>\$1,230</u>

In 2007, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 159 "The Fair Value Option for Financial Assets and Financial Liabilities." SFAS No. 159 allows companies to measure specific financial assets and liabilities at fair value, such as debt or equity investments. The fair value option for the investment in Boston Scientific common stock was applied effective January 1, 2007. Abbott applied the fair value option to its investment in Boston Scientific stock under SFAS No. 159 because, unlike its other equity investments, the Boston Scientific stock is not a strategic investment and Abbott was required to dispose of the stock no later than October 2008. Abbott was subject to a limitation on the amount of shares it may sell in any one month through October 2007 and Abbott did not reacquire the Boston Scientific shares it sold. Accordingly, since at adoption, realized gains or losses were expected in the near future, the fair value option better represented the near-term expected earnings impact from sales of the stock. Under the fair value option, any cumulative unrealized gains or losses on an equity investment previously accounted for as an available-for-sale security is recorded as a cumulative effect adjustment to retained earnings as of the date of adoption of the standard. The pretax and after tax adjustment to Earnings employed in the business upon adoption was \$297 million and

\$189 million, respectively, and the fair value and carrying amount of the investment before and after adoption was approximately \$1.0 billion. The pretax and after tax adjustment to Accumulated other comprehensive income (loss) was \$303 million and \$182 million, respectively. The effect of the adoption on deferred income taxes was not significant.

As described in footnote 3, Abbott recorded a gain of approximately \$94 million in connection with the dissolution of the TAP Pharmaceutical Products Inc. joint venture in 2008, which is included in Other (income) expense, net. Other (income) expense, net for 2008 also includes a gain of approximately \$52 million on the sale of an equity investment accounted for as an available-for-sale investment. The remainder of Other (income) expense, net for 2008 relates primarily to contractual payments based on specified development, approval and commercial events being achieved with respect to products retained by Takeda and payments from Takeda based on sales of products retained by Takeda. Other (income) expense, net for 2007 includes a \$190 million fair market value loss adjustment to Abbott's investment in Boston Scientific common stock and a realized gain of \$37 million on the sales of Boston Scientific common stock. Other (income) expense, net for 2007 and 2006 includes fair value gain adjustments of

#### Note 2 — Supplemental Financial Information (Continued)

\$28 million and \$91 million, respectively, to certain derivative financial instruments included with the investment in Boston Scientific common stock.

	2008	2007	2006
	(dollars in millions)		
<b>Other Accrued Liabilities:</b>			
Accrued rebates payable to government agencies	\$ 577	\$ 662	\$ 661
Accrued other rebates (a)	455	444	391
All other	3,185	2,607	2,799
<b>Total</b>	<b>\$4,217</b>	<b>\$3,713</b>	<b>\$3,851</b>

(a)

Accrued wholesaler chargeback rebates of \$210, \$157 and \$123 at December 31, 2008, 2007 and 2006, respectively, are netted in trade receivables because Abbott's customers are invoiced at a higher catalog price but only remit to Abbott their contract price for the products.

	2008	2007	2006
	(dollars in millions)		
<b>Post-employment Obligations and Other Long-term Liabilities:</b>			
Defined benefit pension plans and post-employment medical and dental plans for significant plans	\$2,713	\$1,872	\$1,897
All other	1,921	1,472	1,266
<b>Total</b>	<b>\$4,634</b>	<b>\$3,344</b>	<b>\$3,163</b>

	(dollars in millions)		
Comprehensive Income, net of tax:			
Foreign currency (loss) gain translation adjustments	\$(2,208)	\$1,153	\$1,039
Net actuarial (losses) gains and prior service cost and credits and amortization of net actuarial losses and prior service cost and credits, net of taxes of \$638 in 2008 and \$(226) in 2007	(987)	343	—
Unrealized (losses) gains on marketable equity securities, net of taxes of \$28 in 2008, \$(31) in 2007 and \$119 in 2006	(49)	54	(178)
Net adjustments for derivative instruments designated as cash flow hedges	(2)	(40)	37
Other comprehensive (loss) income	(3,246)	1,510	898
Net Earnings	<u>4,881</u>	<u>3,606</u>	<u>1,717</u>
Comprehensive Income	<u><u>\$ 1,635</u></u>	<u><u>\$5,116</u></u>	<u><u>\$2,615</u></u>

	2008		2007
	(dollars in millions)		
<b>Supplemental Accumulated Other Comprehensive Income Information,</b>			
net of tax:			
Cumulative foreign currency translation (gain) adjustments	\$ (740)	\$(2,948)	\$(1,795)
Net actuarial losses and prior service cost and credits	1,901	914	1,257
Cumulative unrealized (gains) loss on marketable equity securities	(17)	(66)	169
Cumulative losses (gain) on derivative instruments designated as cash flow hedges	20	18	(21)

---

**Note 2 — Supplemental Financial Information (Continued)**

On December 31, 2006, Abbott adopted the provisions of SFAS No. 158 "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans." Adoption of this statement resulted in a decrease in Abbott's shareholders' equity of \$1.3 billion net of taxes of approximately \$733 million.

	2008		2007
	(dollars in millions)		
<b>Supplemental Cash Flow Information:</b>			
Income taxes paid	\$772	\$952	\$1,282
Interest paid	561	564	429

For the acquired *Lupron* business in 2008, as discussed in footnote 3, Abbott recorded intangible assets, primarily *Lupron* product rights, of approximately \$700 million, goodwill of approximately \$350 million and deferred tax liabilities related to the intangible assets of approximately \$260 million. Abbott also recorded a liability of approximately \$1.1 billion relating to an agreement to remit cash to Takeda if certain research and development events are not achieved on the development assets retained by Takeda. Related deferred tax assets of approximately \$410 million were also recorded, resulting in an after-tax liability of approximately \$700 million. The sale of Abbott's equity interest in TAP resulted in the recording of net assets related to the *Lupron* business, primarily cash, receivables, inventory and other assets, net of accounts payable and other accrued liabilities, offset by a credit to Abbott's investment in TAP in the amount of approximately \$280 million.

**Note 3 — Conclusion of TAP Pharmaceutical Products Inc. Joint Venture and Sale of Abbott's Spine Business**

On April 30, 2008, Abbott and Takeda concluded their TAP Pharmaceutical Products Inc. (TAP) joint venture, evenly splitting the value and assets of the joint venture. Abbott exchanged its 50 percent equity interest in TAP for the assets, liabilities and employees related to TAP's *Lupron* business. Subsequent to the conclusion of the joint venture, TAP was merged into two Takeda entities. The exchange of Abbott's investment in TAP for TAP's *Lupron* business resulted in a gain at closing of approximately \$94 million. The Internal Revenue Service has issued a private letter ruling that the transaction qualifies as tax-free for U.S. income tax purposes.

Beginning on May 1, 2008, Abbott began recording U.S. *Lupron* net sales and costs in its operating results and no longer records income from the TAP joint venture. TAP's sales of *Lupron* were \$182 million for the four months ended April 30, 2008 and \$645 million and \$662 million in 2007 and 2006, respectively. Abbott also receives payments based on specified development, approval and commercial events being achieved with respect to products retained by Takeda and payments from Takeda based on sales of products retained by Takeda, which are recorded by Abbott as Other (income) expense, net as earned. Such payments, which are subject to tax, are expected to approximate \$1.4 billion over the five-year period beginning on May 1, 2008.

The exchange transaction was accounted for as a sale of Abbott's equity interest in TAP and as an acquisition of TAP's *Lupron* business under SFAS No. 141 "Business Combinations." The sale of Abbott's equity interest in TAP resulted in the recording of net assets related to the *Lupron* business, primarily cash, receivables, inventory and other assets, net of accounts payable and other accrued liabilities, offset by a credit to Abbott's investment in TAP in the amount of approximately \$280 million.

For the acquired *Lupron* business, Abbott recorded intangible assets, primarily *Lupron* product rights, of approximately \$700 million, goodwill of approximately \$350 million and deferred tax liabilities related primarily to the intangible assets of approximately \$260 million. The intangible assets are being amortized over 15 years. Abbott has also agreed to remit cash to Takeda if certain research and development events

---

**Note 3 — Conclusion of TAP Pharmaceutical Products Inc. Joint Venture and Sale of Abbott's Spine Business (Continued)**

are not achieved on the development assets retained by Takeda. These amounts were recorded as a liability at closing in the amount of approximately \$1.1 billion. Related deferred tax assets of approximately \$410 million were also recorded, resulting in an after-tax liability of approximately \$700 million. Of the \$1.1 billion, Abbott made a tax-deductible payment of \$200 million in 2008 and Abbott will make a tax-deductible payment of approximately \$120 million in 2009. If the remaining payments are not required, the liability would be reduced and a gain would be recorded.

The 50 percent-owned joint venture was accounted for under the equity method of accounting. Summarized financial information for TAP follows below. The results for 2008 include results through April 30. (*dollars in millions*)

	<u>2008</u>	<u>2007</u>	<u>2006</u>
Net sales	\$853	\$3,002	\$3,363
Cost of sales	229	720	836
Income before taxes	356	1,564	1,524
Net income	238	996	952

In the fourth quarter of 2008, Abbott sold its spine business for approximately \$360 million in cash, resulting in an after-tax gain of approximately \$147 million which is presented as Gain on sale of discontinued operations, net of taxes, in the accompanying statement of income. The operations and financial position of the spine business are not presented as discontinued operations because the effects would not be significant.

#### **Note 4 — Financial Instruments, Derivatives and Fair Value Measures**

Certain Abbott foreign subsidiaries enter into foreign currency forward exchange contracts to manage exposures to changes in foreign exchange rates for anticipated intercompany purchases by those subsidiaries whose functional currencies are not the U.S. dollar. These contracts, totaling \$129 million, \$281 million and \$768 million at December 31, 2008, 2007 and 2006, respectively, are designated as cash flow hedges of the variability of the cash flows due to changes in foreign exchange rates. Abbott records the contracts at fair value, resulting in charges of \$2 million and \$12 million in 2008 and 2007, respectively, and a credit of \$16 million to Accumulated other comprehensive income (loss) in 2006. Ineffectiveness recorded in 2008, 2007 or 2006 was not significant. Accumulated gains and losses as of December 31, 2008 will be included in Cost of products sold at the time the products are sold, generally through the next twelve months.

Abbott enters into foreign currency forward exchange contracts to manage currency exposures for foreign currency denominated third-party trade payables and receivables, and for intercompany loans and trade accounts payable where the receivable or payable is denominated in a currency other than the functional currency of the entity. For intercompany loans, the contracts require Abbott to sell or buy foreign currencies, primarily European currencies and Japanese yen, in exchange for primarily U.S. dollars and other European currencies. For intercompany and trade payables and receivables, the currency exposures are primarily the U.S. dollar, European currencies and Japanese yen. These contracts are recorded at fair value, with the resulting gains or losses reflected in income as Net foreign exchange (gain) loss. At December 31, 2008, 2007 and 2006, Abbott held \$8.3 billion, \$5.5 billion and \$5.6 billion, respectively, of such foreign currency forward exchange contracts.

Abbott has designated foreign denominated short-term debt as a hedge of the net investment in certain foreign subsidiaries of approximately \$585 million and approximately \$1.7 billion as of

---

#### **Note 4 — Financial Instruments, Derivatives and Fair Value Measures (Continued)**

December 31, 2008 and 2007, respectively. Accordingly, changes in the fair value of this debt due to changes in exchange rates are recorded in Accumulated other comprehensive income (loss), net of tax, resulting in charges of \$134 million and \$72 million to Accumulated other comprehensive income (loss) in 2008 and 2007, respectively.

Abbott is a party to interest rate hedge contracts totaling \$2.5 billion at December 31, 2008 and \$1.5 billion at December 31, 2007 and 2006 to manage its exposure to changes in the fair value of \$2.5 billion and \$1.5 billion, respectively, of fixed-rate debt due 2009 through 2017. These contracts are designated as fair value hedges of the variability of the fair value of fixed-rate debt due to changes in the long-term benchmark interest rates. The effect of the hedge is to change a fixed-rate interest obligation to a variable rate for that portion of the debt. Abbott records the contracts at fair value and adjusts the carrying amount of the fixed-rate debt by an offsetting amount. No hedge ineffectiveness was recorded in income in 2008, 2007 and 2006.

Gross unrealized holding gains (losses) on available-for-sale equity securities totaled \$55 million and \$(23) million, respectively, at December 31, 2008; \$108 million and \$(3) million, respectively, at December 31, 2007 and \$21 million and \$(304) million, respectively, at December 31, 2006.

The carrying values and fair values of certain financial instruments as of December 31 are shown in the table below. The carrying values of all other financial instruments approximate their estimated fair values. The counter parties to financial instruments consist of select major international financial institutions. Abbott does not expect any losses from nonperformance by these counter parties.

	2008		2007		2006	
	Carrying Value	Fair Value	Carrying Value	Fair Value	Carrying Value	Fair Value
<b>Current Investments:</b>						
Available-for-Sale Equity Securities	\$ —	\$ —	\$ —	\$ —	\$ 775	\$ 775
Trading Securities			308	308		
Other	968	968	56	56	77	77
<b>Long-term Investments:</b>						
Available-for-Sale Equity Securities	147	147	229	229	378	378
Note Receivable	865	824	851	809	837	849
Other	62	56	45	40	15	15
Total Long-term Debt	(9,754)	(10,458)	(10,386)	(10,593)	(7,105)	(7,113)
<b>Foreign Currency Forward Exchange Contracts:</b>						
Receivable position	148	148	24	24	34	34
(Payable) position	(100)	(100)	(45)	(45)	(86)	(86)
Interest Rate Hedge Contracts	170	170	(25)	(25)	(85)	(85)

---

#### Note 4 — Financial Instruments, Derivatives and Fair Value Measures (Continued)

The following table summarizes the bases used to measure certain assets and liabilities at fair value on a recurring basis in the balance sheet: (*dollars in millions*)

	Outstanding Balances	Basis of Fair Value Measurement		
		Quoted Prices in Active Markets	Significant Other Observable Inputs	Significant Unobservable Inputs
<b>December 31, 2008:</b>				
Equity and other securities	\$ 144	\$ 105	\$ 10	\$ 29

Foreign currency forward exchange contracts	148	—	148	—
Interest rate swap financial instruments	170	—	170	—
Financial assets relating to TAP employees' stock options	16	—	16	—
Total Assets	\$ 478	\$ 105	\$ 328	\$ 45
Fair value of hedged long-term debt	\$ 2,670	\$ —	\$ 2,670	\$ —
Foreign currency forward exchange contracts	100	—	100	—
Financial liabilities relating to TAP employees' stock options	24	—	24	—
Total Liabilities	\$ 2,794	\$ —	\$ 2,770	\$ 24
December 31, 2007:				
Trading securities	\$ 308	\$ 308	\$ —	\$ —
Marketable available-for-sale securities	193	193	—	—
Foreign currency forward exchange contracts	24	—	24	—
Total Assets	\$ 525	\$ 501	\$ 24	\$ —
Fair value of hedged long-term debt	\$ 1,475	\$ —	\$ 1,475	\$ —
Interest rate swap financial instruments	25	—	25	—
Foreign currency forward exchange contracts	45	—	45	—
Total Liabilities	\$ 1,545	\$ —	\$ 1,545	\$ —

In connection with the conclusion of the TAP Pharmaceutical Products Inc. joint venture, Abbott recorded derivative financial assets and liabilities related to stock options previously granted to TAP's employees. The amounts of these assets and liabilities were calculated using both the Black-Scholes option-pricing model and the intrinsic value of the options. From April 30, 2008 to December 31, 2008, both the assets and liabilities decreased by approximately \$29 million. The effect of the changes in these assets and liabilities substantially offset each other. In addition, Abbott received investments in 2008 that are valued using significant unobservable inputs. The recorded value of these investments did not change significantly. In 2007, adjustments to record a derivative financial instrument liability whose value was derived using significant unobservable inputs resulted in a credit to Other (income) expense, net, in the amount of \$25 million. The value of this derivative financial instrument liability was zero at December 31, 2007.

---

#### Note 5 — Post-Employment Benefits

Retirement plans consist of defined benefit, defined contribution and medical and dental plans. Information for Abbott's major defined benefit plans and post-employment medical and dental benefit plans is as follows: (*dollars in millions*)

	Defined Benefit Plans			Medical and Dental Plans		
	2008	2007	2006	2008	2007	2006
Projected benefit obligations, January 1	\$ 5,783	\$ 5,614	\$ 5,041	\$ 1,514	\$ 1,520	\$ 1,292
Service cost — benefits earned during the year	233	249	219	43	58	56
Interest cost on projected benefit obligations	353	316	275	92	97	80
Losses (gains), primarily changes in discount and medical cost trend rates, plan design changes, law changes and differences between actual and estimated health care costs	(278)	(309)	64	(158)	(100)	134
Benefits paid	(241)	(228)	(213)	(68)	(61)	(68)
Other, primarily foreign currency translation	(309)	141	228	20	—	26
Projected benefit obligations, December 31	\$ 5,541	\$ 5,783	\$ 5,614	\$ 1,443	\$ 1,514	\$ 1,520